

# The Economic and Fiscal Outlook, **FY 2004 and FY 2005**

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Presented to  
Tennessee State Funding Board

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## I. National Summary

1. The economic outlook appears brighter for 2004. The balance of the economic scale is tilting toward the positive.
2. Expect the economic news to continue to be mixed:

### Positive Factors

- ◆ Stimulative policies slowly taking effect.
- ◆ Seven quarters of uneven but positive economic growth. Third quarter GDP increased 8.2 percent.
- ◆ Corporations reporting some profits.
- ◆ Strong rebound in consumer confidence.
- ◆ Capital spending weak but improved.
- ◆ Little or no inflation (2.0 percent) or deflation.
- ◆ Productivity high.
- ◆ Inventories low.
- ◆ Tech sector leading stock market gains.
- ◆ Stable low interest rate.
- ◆ Oil prices somewhat lower although in a state of fluctuation.

### Negative Factors

- ◆ Little or no job growth with the recovery.
- ◆ Manufacturing base continues to disappear.
- ◆ Relatively high unemployment.
- ◆ Health care costs continue to rise.
- ◆ Welfare roles are increasing.
- ◆ Threats ... and risk are high.
- ◆ Drain of the wars continues with no end in sight.
- ◆ Gold prices rising along with uncertainty.
- ◆ Weak international markets.
- ◆ Deficits are running high.
- ◆ Corporate and stock market scandals continue.
- ◆ GDP growth unsustainable.
- ◆ Interest rates expected to increase.

- ◆ Value of the dollar is falling so exports are beginning to increase.
- ◆ Personal income figures are up (3.3 percent increase for July 2003 over July 2002).
- ◆ Retail sales reports indicate good news (up 5.4 percent for year-to-date 2003 versus 2002).
- ◆ State and local government budgets are improving.

## II. Summary for Memphis

### Positive Factors

- ◆ Job losses have been small and may turn positive as economy rebounds.
- ◆ Memphis is a slow-and-steady growth town with a small manufacturing base.
- ◆ Personal income figures continue to rise.
- ◆ Strong housing sector leads the economy.
- ◆ Biotech is a fine long-term strategy.
- ◆ Memphis is a stable community with manageable growth problems.

### Negative Factors

- ◆ Three years of job stagnation has increased poverty, welfare caseloads, and discouraged workers.
- ◆ Some activities are clearly being left behind by cyclical and structural changes in job opportunities.
- ◆ Shelby County continues to suffer with a high debt load and limited revenues.
- ◆ The wind storm was a major economic setback.

### III. Summary for Tennessee

#### Positive Factors

- ◆ Economic recovery will have a positive impact on employment and earnings in Tennessee.
- ◆ Consumer confidence increases and retail sales growth will be good news for sales taxes.
- ◆ Tennessee's farmers and local markets will benefit from improved prices and outputs.
- ◆ The job and income gains in urban areas continue to lead the state.
- ◆ The growth of the auto industry continues to stimulate the economy.
- ◆ The growth in stock values should increase expenditures from wealth and taxes on unearned income.

#### Negative Factors

- ◆ The loss of manufacturing jobs is particularly severe for rural counties.
- ◆ High unemployment rates in rural counties will be difficult to reduce.
- ◆ Poverty rates and welfare caseloads are rising.
- ◆ The cost of health care continues to absorb any revenue increases.
- ◆ Tuition increases for higher education will impact enrollments.
- ◆ State revenue growth will return to the long-term growth rate.

## IV. Collections Forecast

- Forecasts of total collections for FY 2004 (August 2003 through July 2004) call for 7.0 percent growth, followed by 3.9 percent growth for FY 2005.
- The estimated risk that end-of-year collections will be less than the budget target, a 0.07 probability, is very low in comparison to previous years' risks.
- Sales and use taxes are forecast to grow 5.6 percent for 2004, then 3.2 percent in 2005. The risk of a shortfall relative to the budget target is small.
- Franchise and excise tax collections have been very erratic in the past six years and are forecast to grow more than targeted in the 2004 budget. Their anticipated growth would put them at levels at or above historical highs.
- Income taxes are forecast to show no growth in FY 2004. However, that is good performance, given the 19.0 percent decrease seen in 2003 and the 41.0 percent cumulative drop since 2000. The risk analysis indicates a relatively high probability that income tax collections will be short of the budget target.
- The three-decade trend of an increase in the dependence on the sales and use tax for financing Tennessee state government moved above 64.0 percent in FY 2003.

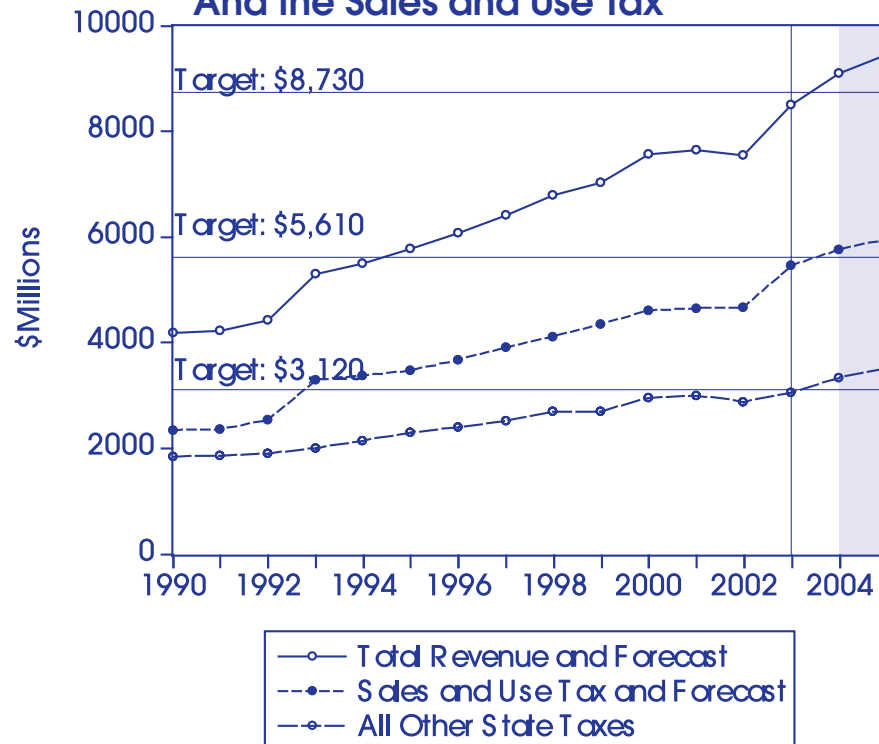
**Table 1. Collections and Forecasts for August Through July Fiscal Year  
(\$Millions)**

|                            | 2003 FY         |              | Forecast for 2004 |             | Forecast for 2005 |             |
|----------------------------|-----------------|--------------|-------------------|-------------|-------------------|-------------|
|                            | Amount          | Growth       | Amount            | Growth      | Amount            | Growth      |
| Franchise                  | \$ 484.8        | 12.4%        | \$ 557.0          | 14.9%       | \$ 601.0          | 7.9%        |
| Excise                     | 600.2           | 11.7%        | 646.6             | 7.7%        | 697.0             | 7.8%        |
| Income                     | 116.8           | -19.2%       | 117.0             | 0.2%        | 136.4             | 16.6%       |
| Inheritance and Estate     | 81.8            | -16.1%       | 104.9             | 28.3%       | 99.9              | -4.8%       |
| Gasoline                   | 600.9           | 4.2%         | 607.1             | 1.0%        | 613.3             | 1.0%        |
| Petroleum Special          | 60.7            | -1.5%        | 62.5              | 3.0%        | 64.4              | 3.0%        |
| Tobacco                    | 114.5           | 33.5%        | 114.6             | 0.1%        | 114.7             | 0.1%        |
| Beer                       | 17.7            | 12.6%        | 16.5              | -7.1%       | 17.1              | 3.9%        |
| Motor Vehicle Registration | 226.8           | 2.5%         | 236.9             | 4.4%        | 247.3             | 4.4%        |
| Motor Vehicle Title        | 11.0            | 3.1%         | 11.4              | 3.5%        | 11.8              | 3.5%        |
| Mixed Drink                | 38.5            | 7.7%         | 40.2              | 4.6%        | 42.4              | 5.2%        |
| Business                   | 40.3            | 90.9%        | 97.0              | 140.9%      | 97.5              | 0.5%        |
| Privilege                  | 248.6           | 19.6%        | 297.3             | 19.6%       | 326.4             | 9.8%        |
| TVA and Gross Receipts     | 216.3           | -3.4%        | 222.6             | 2.9%        | 229.0             | 2.9%        |
| Alcoholic Beverage         | 34.7            | 13.2%        | 35.3              | 1.7%        | 35.9              | 1.7%        |
| Sales and Use              | 5,455.2         | 17.2%        | 5,763.2           | 5.6%        | 5,946.8           | 3.2%        |
| Motor Vehicle Fuel         | 154.8           | -12.9%       | 170.4             | 10.1%       | 175.3             | 2.9%        |
| Severance                  | 1.1             | -5.5%        | 1.0               | -4.5%       | 1.0               | -4.4%       |
| Coin-operated Amusement    | 0.8             | 5,642%       | 0.8               | 0.0%        | 0.8               | -0.1%       |
| <b>Total</b>               | <b>\$ 8,505</b> | <b>12.9%</b> | <b>\$ 9,102.4</b> | <b>7.0%</b> | <b>\$ 9,457.9</b> | <b>3.9%</b> |

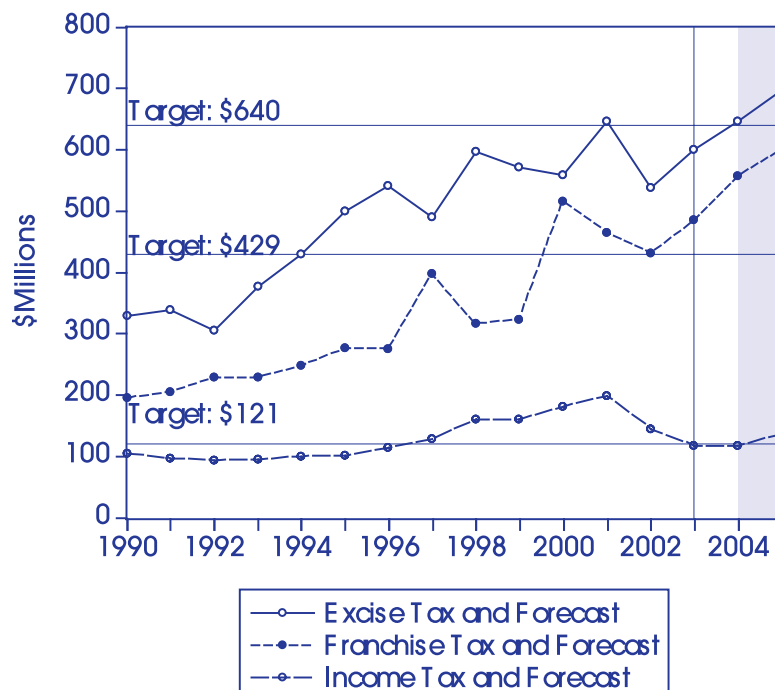
**Table 2. Risk Analysis for 2004 Fiscal Year Collections, August Through July (\$Millions)**

|                            | 2003              | 2004              | Median            | Difference       | Probability  |
|----------------------------|-------------------|-------------------|-------------------|------------------|--------------|
|                            | Actual            | Target            | Forecast          | Forecast-Target  | Below Target |
| Franchise                  | \$ 484.8          | \$ 428.8          | \$ 557.0          | \$ 128.2         | 0.01         |
| Excise                     | 600.2             | 639.8             | 646.6             | 6.8              | 0.46         |
| Income                     | 116.8             | 121.1             | 117.0             | -4.1             | 0.65         |
| Inheritance and Estate     | 81.8              | 75.0              | 104.9             | 29.9             | 0.14         |
| Gasoline                   | 600.9             | 588.5             | 607.1             | 18.6             | 0.05         |
| Petroleum Special          | 60.7              | 64.7              | 62.5              | -2.2             | 0.84         |
| Tobacco                    | 114.5             | 118.4             | 114.6             | -3.8             | 1.00         |
| Beer                       | 17.7              | 18.0              | 16.5              | -1.5             | 0.99         |
| Motor Vehicle Registration | 226.8             | 240.8             | 236.9             | -3.9             | 0.68         |
| Motor Vehicle Title        | 11.0              | 11.1              | 11.4              | 0.3              | 0.30         |
| Mixed Drink                | 38.5              | 39.9              | 40.2              | 0.3              | 0.23         |
| Business                   | 40.3              | 96.4              | 97.0              | 0.6              | 0.34         |
| Privilege                  | 248.6             | 249.6             | 297.3             | 47.7             | 0.03         |
| TVA and Gross Receipts     | 216.3             | 224.0             | 222.6             | -1.4             | 0.57         |
| Alcoholic Beverage         | 34.7              | 35.0              | 35.3              | 0.3              | 0.22         |
| Sales and Use              | 5,455.2           | 5,609.6           | 5,763.2           | 1,53.6           | 0.07         |
| Motor Vehicle Fuel         | 154.8             | 165.1             | 170.4             | 5.3              | 0.31         |
| Severance                  | 1.1               | 1.1               | 1.0               | -0.1             | 0.70         |
| Coin-operated Amusement    | 0.8               | 3.5               | 0.8               | -2.7             | 1.00         |
| <b>Total</b>               | <b>\$ 8,505.3</b> | <b>\$ 8,730.4</b> | <b>\$ 9,102.4</b> | <b>\$ 3,72.0</b> | <b>0.07</b>  |

**Figure 1: Forecasts and Trends Relative to 2004  
Budget Targets for Total Tax Revenue  
And the Sales and Use Tax**



**Figure 2: Forecasts and Trends Relative to 2004  
Budget Targets for Excise, Franchise,  
And Income Taxes**



**Figure 3: Trend in the Proportion of Total  
Tennessee State Taxes Contributed by  
The Sales and Use Tax**

